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MARKET TRENDS AND COMMODITY DEVELOPMENT FOR COTTON

Study by the UNCTAD secretariat

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I. INTRODUCTION

1. This report gives a brief review of main trends in markets for cotton since the early 1980s and of recent developments in the areas of further processing of cotton, generic market promotion, research and development and price formation in world markets.

2. In a development context, cotton is important for income and employment provided in its production and processing in developing countries as well as for the foreign exchange earnings on its exports. An estimated 200 million people in developing countries gain all or part of their cash income from growing cotton. As a light industry which can utilize simple known technology, yarn and textile manufacturing has served as one of the first industries in the industrialization process. About 50 million people are employed in its processing in developing countries. The people growing and processing cotton represent about 7 per cent of the total population of all developing countries. Developing countries earned $US 3.5 billion on exports of raw cotton in 1990. Exports of cotton yarn totalled more than $US 2.7 billion for these countries in the same year. Cotton is grown for cash income in tropical and temperate regions in more than 85 countries, and is exported in significant quantities from more than a third of them. Most cotton producing countries are low to middle income developing countries. For 12 countries, raw cotton exports account for 15 per cent or more of their total export earnings and four countries, Benin, Burkina Faso, Chad and Mali, depend on raw cotton for over 40 per cent of their export earnings.

II. REVIEW OF MARKET TRENDS

A. Global trends

1. World production and consumption

3. World production and consumption of cotton have risen considerably in the 1981-1993 period as seen in Chart 1. Production fluctuated around the trend more than did consumption. Both production and consumption are expected to continue to increase in the years to come.

4. Five economies, China, the CIS, the United States, India and Pakistan, account for three fourths of world cotton production. The share of developing countries has increased during the past few decades due to a large increase in productivity. In the CIS, the largest cotton producing republic is Uzbekistan with almost two-thirds of CIS production. Turkmenia accounts for almost one fifth. The other large producers are Tadzhikistan and Azerbaijan.

5. A little more than one quarter of world production enters international trade as raw cotton exports, not counting trade within the CIS. The share would be much higher if cotton yarn and textiles were included in exports.

6. As regards consumption, China, India, the CIS and the United States account for over half of total cotton consumption at the level of mills that spin and weave it. Developed market economy countries account for somewhat over one fourth of raw cotton consumption by mills, but for close to one third of final consumption of cotton with yarns and textiles included.

2. World cotton trade

7. The major cotton producing economies also account for a large part of raw cotton exports. The CIS, the United States, Pakistan and China account for two thirds of projected exports for 1993. The levels of their exports over the period 1981 to 1993 are seen in Chart 2. The "other countries" group is mostly comprised of developing countries whose production is largely for exports and which rely on cotton for a major part of their total export earnings. Some cotton producing developing countries have expanded their exports of cotton yarn and textiles. The value of cotton yarn exports now exceeds that of raw cotton exports in Pakistan, Egypt, China and Brazil. The trend toward further processing of cotton is expected to continue as producing countries seek to gain the value added from this industry.

8. Imports of raw cotton are strongly concentrated. The EEC alone accounts for more than one fifth of cotton imports. Other important importers of raw cotton are Japan and the countries of East and South-East Asia in particular, Taiwan Province of China, the Republic of Korea, Indonesia, Hong Kong and Thailand. China started importing large quantities only in 1989.

3. Price developments

9. Chart 3 illustrates the movements in prices of three different kinds of cotton, CIF Northern Europe. The prices remained fairly stable through the 1960s to 1972. They shot up sharply with the "commodity boom" in 1973 and have fluctuated strongly since then. A sharp fall occurred in the period from 1980 to 1986, with some recovery since.

10. The price relation between the US Memphis territory M 1-3/32 inch and the very similar Central American M 1-3/32 inch seems to have widened and become more unstable. That of the quite different Sudan Barakat X4B, a fine long staple, moved differently from the other two.

11. Cotton yarn prices develop to some extent independently from raw cotton prices. In the United States, the price spread fluctuated between 80 and 120 cents per pound in the 1986-1992 period. In Japan, the spread fluctuated between 90 and 200 yen per pound in the same period.

12. Large production in the 1984/85 and 1985/86 crop seasons lead to oversupply, large stocks and low prices. A strong growth in consumption in 1986 and continued high consumption thereafter resulted in the limited price improvement, but prices have weakened since 1990.

13. World cotton prices are still at depressed levels. Strong concern was expressed about the depressed world prices for cotton at the 51st Plenary Meeting of the International Cotton Advisory Committee in October 1992. At that Meeting, a number of producing countries pointed out that the burden of adjustment falls heavily on producers, particularly in those countries with no or limited government support, and some developing countries highly dependent on cotton growing where growing conditions were unfavourable for alternative crops were facing economic and social disruption of crisis proportions.

Chart 1
World cotton consumption, production and exports

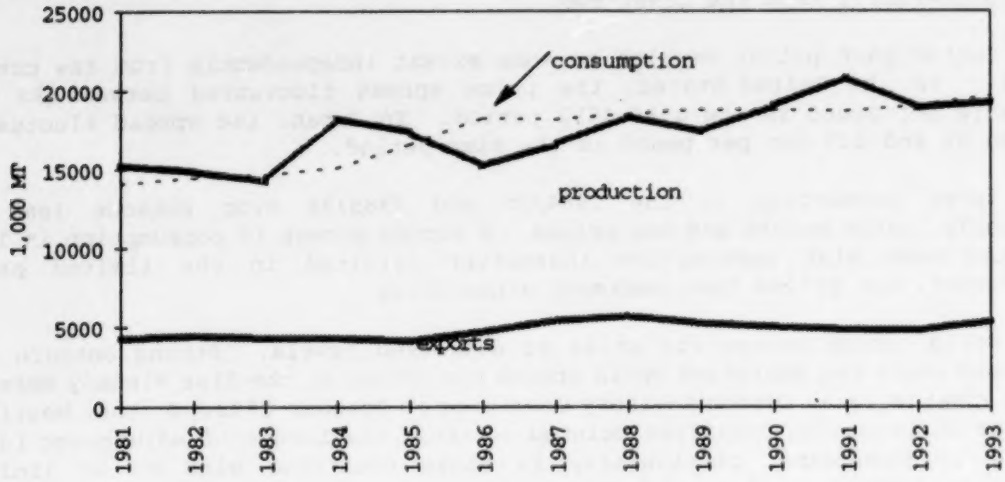


Chart 2
World cotton exports

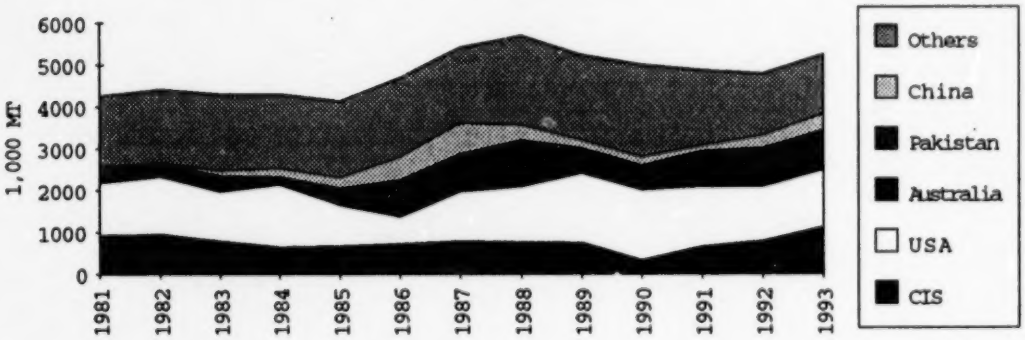
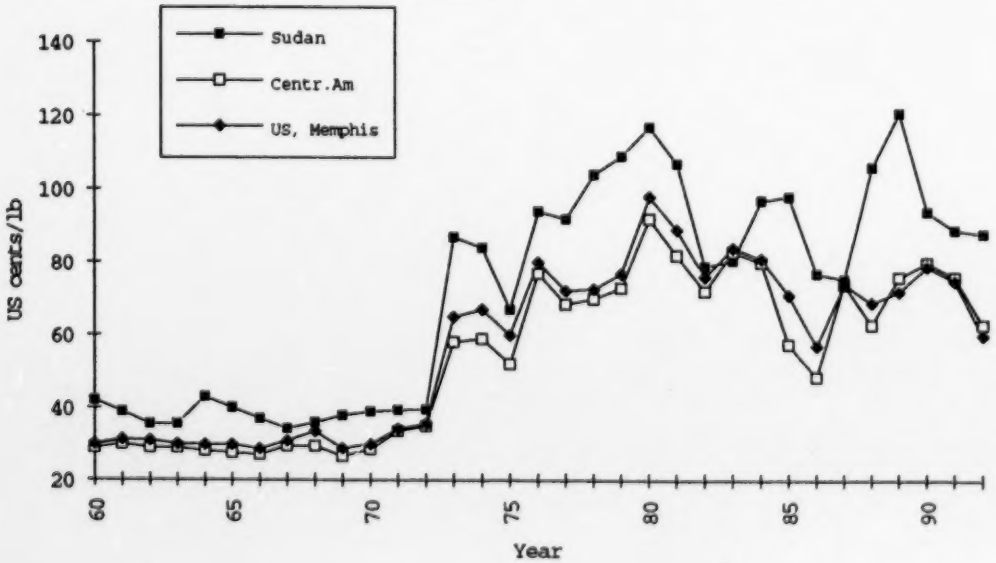


Chart 3
Cotton prices, CIF Europe, US cents/lb



B. Salient features of supply

14. World production of cotton increased from 14.1 million metric tonnes in the 1980/81 season (1 August to 31 July) to 18.4 million mt in 1992/93, as yields increased greatly while harvested area rose only slightly. Total exports of raw cotton paralleled the growth in production, rising from 4.3 million mt to 5.8 million mt in the period.

15. Africa's production edged upward from 1,152,000 mt to 1,262,000 mt in the period. However, a major shift occurred as Egypt's production dropped from nearly half of the continent's total to little more than one fourth while production increased in many small producing countries such as Benin, Burkina Faso, Côte d'Ivoire, Mali, Senegal, United Republic of Tanzania and Togo. Egypt's drop in production was due to a fall in harvested area while other producing countries had strong increases in yields and varying experiences with harvested area. Africa's exports rose from 565,000 mt in 1980/81 to 658,000 mt in 1992/93. A fall in Egypt's exports was outmatched by increases in those of the small producing countries which had rises in production.

16. Production and exports of raw cotton have dropped sharply in Mexico and the Central American countries. The levels which stood at 612,000 mt for production and 392,000 mt for exports in 1980/81 plunged to 63,000 mt and a mere 19,000 mt respectively in 1992/93.

17. South America's production increased slightly from 1,056,000 mt to 1,149,000 mt and exports from 205,000 mt to 270,000 mt in the 1980/81 to 1992/93 period. Some countries had increases in production and exports, notably Argentina and Paraguay, while others had decreases, particularly Colombia and Peru.

18. In the developing countries of Asia including Turkey but excluding China and the Central Asian republics of the CIS, production sharply increased from 2,861,000 mt to 4,850,000 mt in the period, mainly due to the huge increases of India and Pakistan but also some increases in a few other countries. India's rise was due solely to yield while Pakistan's was due to yield and, to a lesser extent, area. Exports of cotton from these developing countries of Asia jumped from 785,000 mt to 939,000 mt, as India, Pakistan and Syria increased their levels.

19. China had a tremendous increase in production in the period, rising from 2,707,000 mt in 1980/81 to 4,740,000 in 1992/93, due to large increases in both yield and area. Exports jumped from none to 200,000 mt.

20. Production in the CIS dropped from the level of 2,866,000 mt as the former Soviet Union to 2,079,000 mt over the 1980/81 to 1992/93 period, as yield fell and area did too but to a lesser extent. Exports to countries outside of the former Soviet Union, at 800,000 in 1992/93, are at the level of the 1980/81 season.

21. The United States had a huge increase in production from 2,422,000 mt in 1980/81 to 3,540,000 mt in 1992/93, due to a large increase in yield while harvested area fell. Exports rose from 1,290,000 mt to 1,372,000 mt.

22. Australia's production jumped from 99,000 mt to 325,000 mt in the period as both yield and area increased greatly. Exports followed with a sharp rise from 53,000 mt to 329,000 mt.

C. Salient features of demand

23. The evolution of demand for cotton has been favourable to the commodity over the past decade, despite strong competition from man-made fibres. Cotton has increased its market share to nearly one half of global fibre consumption and its consumption has risen steadily. Demand is expected to remain strong especially for high quality cotton.

24. The main factors explaining the positive performance of cotton are rising income levels, population growth and preferences of consumers.

25. The evolution of demand for cotton, on an end-use basis of final consumption, has differed from one region to another. Growth of consumption has been low in Eastern Europe as compared to the OECD countries. Also, cotton's share of all fibre consumption declined in the former while increasing in the latter.

26. Developing countries consume, on an end-use basis, about half of the world consumption. Consumption has been rising in these countries due largely to population growth. There are considerable differences in cotton's market shares among these countries. Shares of cotton are high in, for example, India and Pakistan compared to some other countries which have synthetic fibre production capacity and more vigorous competition.

27. The use of blends of synthetics and cotton differ from group to group. In developed countries, normal blends are typically 50/50 or 65/35 in favour of polyester. In developing countries blends are more rare and most fabrics are either all synthetic or all cotton.

28. Demand for cotton may be categorized into three general classes of end-uses: clothing, household uses and industrial uses.

29. Clothing is the main end-use. Cotton's market share in clothing has been increasing over the past two decades. More than half of total cotton consumption in industrialized countries is consumed as clothing even though the share of cotton in total fibre consumption is only about one third in the EEC and about 43 per cent in the United States. Clothing is a sector where fashion and subjective appeal as well as comfort, easy care and durability are important considerations for consumers.

30. Household uses is the next largest category in cotton consumption. Towels and bed linens are the largest end-uses as absorbency is a major factor and cotton's performance is good.

31. Cotton has not competed well in industrial uses, the smallest of the three categories of end-uses. Technical factors, such as abrasion resistance are important in industrial uses. Another factor is that the length of synthetic fibres can be adjusted to suit specific industrial requirements. In some applications, for example for automotive tyres, synthetics have completely replaced cotton.

32. Cotton's first competitors were the cellulostics, rayon and acetate. Since some of their characteristics were quite different from cotton, severe competition came only with the development of non-cellulostics, mainly polyester but also acrylic and nylon. Polyester met consumer preferences for easy care and abrasion resistance while presenting an appearance close to that of cotton. Blends of the two fibres have been used to obtain desirable qualities of both.

33. Competition with man-made fibres is not only a matter deriving from choices of final consumers. Decisions of spinners, within some limits, are also of importance in determining shares of cotton and the man-made fibres. Generally, for clothing a number of cost components for the final items, for example, design, distribution, and costs of brand names are higher than the cost of the fibres used. However, to a spinner or integrated spinning/weaving enterprise, the choice between fibres can be very sensitive to the fibres' prices since profit margins in spinning are very thin and the raw material constitutes a large part of total cost of manufacturing yarn. Operators will therefore try to minimize total manufacturing cost by choosing the combination of fibres that costs least yet still meets the specifications of contracts.

34. It has often been said that reliability of supply, stability of prices and good customer service are other factors favouring choice of man-made fibres by spinners. Another factor is that man-made fibres can be supplied in standard qualities while cotton, being a natural product, is subject to variations. It should be noted that in recent years grading of cotton has vastly improved with the introduction of high volume instrument (HVI) testing and scientific measurements to replace the more subjective visual techniques used by skilled personnel in the traditional grading systems.

35. Production of synthetic fibres is closely related to the petrochemical industry. Prices of synthetics depend not only on the price of crude oil but also on the pricing of the various petrochemical products where synthetics manufactures buy them or, in the case of integrated operations, the prices at which the transfer takes place. As petrochemicals have many other uses, their prices are not closely related to the demand conditions in the submarket for synthetics production.

36. The world recession has manifested itself in static consumption levels of cotton through the 1990-1992 period. Under normal economic conditions cotton consumption would rise from year to year. Some increase is expected in the 1993/94 season (1 August to 31 July) with an estimated 19.23 million metric tonnes as compared to 18.69 million metric tonnes in 1992/93. The rise is expected due to modest increases in consumption in a number of main countries with the notable exception of the CIS and Eastern Europe where the level is expected to remain unchanged, following sharp falls in 1990 and 1991.

III. FURTHER PROCESSING IN SELECTED DEVELOPING COUNTRIES

37. This chapter presents information on further processing of cotton and changes in trade regimes and policies for development of processing of cotton in five developing countries. They are Egypt, Mexico, Pakistan, Peru and Nigeria.

38. Although situations differ in these countries, they illustrate some new trends in world trade in raw cotton, cotton yarn and cotton fabric as well as imports into cotton producing/exporting countries of these products. These

countries show the greater complexity of the world trade matrix as compared to the simpler situation a decade or two ago of largely raw cotton exports by producing countries.

39. Of these five countries, Pakistan is the leading exporter with yarn slightly higher than raw cotton and fabric being less than either based on calculations by weight. By value, yarn and fabric would be higher than raw cotton in importance. Egypt, the next largest exporter of the three categories, has a heavy predominance in exports of cotton yarn and fabric, calculated by weight and even more so calculated by value. Egypt is also a large importer of raw cotton more than doubling its exports of raw cotton. According to the latest data available, Mexico has small exports of raw cotton and some exports of cotton yarn. Mexico's large imports of raw cotton taken together with cotton fabric imports are 13 times the volume of its raw cotton and yarn exports. Mexico also has large exports of ready-made clothing not counted in these calculations because of difficulty in estimating their weight. According to the most recent figures available, Peru's exports of raw cotton are only a third of its yarn and fabric exports taken together by weight. By value, yarn and cloth are of much greater importance. Peru imports as much raw cotton as it exports. Nigeria is a considerable importer of raw cotton with no exports or trade in yarn or cloth. Nigeria is of interest as a country with a large potential for cotton growing and processing.

40. All of the five countries have considerable cotton production with Pakistan's being the largest by far. Using latest figures available, exports of raw cotton, cotton yarn and cotton fabric net of imports of these categories are expressed as a per cent of production, giving a rough measure of the importance of trade as outlets for domestic cotton production or, in other words, the dependence of the production on trade for off-take. The percentage for Pakistan is highest at 69.8, Peru is next at 56.2. Egypt, with its large population and home market for apparel, has a percentage of 24.1. Nigeria's imports are the equivalent of a third of its domestic production of cotton. Mexico's cotton production has fallen so low that it is perhaps equivalent to only a fourth of its imports. As noted above, Mexico has large exports of clothing items that are not taken into account in these calculations.

1. Egypt

41. Cotton occupies a unique position in the Egyptian economy. As of 1985, it was the major source of cash income for about six million people including cotton farmers, farm workers and their families. In addition, the large spinning and textile industry is of importance for income and employment.

42. Egypt is a large producer of "Extra-Fine" cotton but exports only small quantities as the bulk of the crop is processed in the country. About 30 per cent of production is Extra Long Staple (ELS) having fibres 1-3/8 inches and above, and the remainder is Long Staple (LS) of 1-1/4 inches to less than 1-3/8ths. One-fifth of ELS production was exported in 1991/92 but only 3 per cent of LS output. Being Extra Fine cotton, Egypt's lint, yarn and textiles are of a special high quality. In marketing of raw cotton, ELS and to a lesser extent LS have their own special markets. For example, there is no close relationship between Egyptian cotton prices on world markets and international indicators such as the Cotlook A index or the futures prices on the New York Cotton Exchange.

43. Imports of raw cotton into Egypt are presently more than twice the country's exports. Recently, 85 per cent of imports were US "upland" cotton (California/Acala and California/Arizona).

44. The Government has had for many years a policy of raising prices paid to growers in an attempt to raise cotton production and exports.

45. As of 1985, local cotton consumption by mills was a fundamental objective of Government policy every year because domestic mills were considered to be the principal consumer of Egyptian cotton. The Government's objective was to supply the local mills with all their requirements of cotton varieties and grades at the beginning of each cotton season.

46. Domestic mill consumption increased over the years, mainly due to the Government's planning which aimed to expand cotton industry in order to meet home requirements for the large and growing population as well as to increase exports of cotton yarn and textiles. Egypt's mills consumed only 23 per cent of the crop in the 1950s and 53 per cent in the 1970s rising to 66 per cent in 1984/85. Presently, mill consumption is larger than the crop, since imports are greater than exports. Only 5 per cent of the crop was exported as fibre in 1992/93.

47. From 1985, at the beginning of each season, the Ministry of Foreign Trade announced prices to be paid to growers and as well as those for domestic mills and foreign markets as sales prices. Export firms bought cotton from growers, on behalf of the Government and at the announced prices after deducting ginning and interior marketing expenses, and these companies sold cotton lint at the designated prices to local mills and foreign markets. The Government set the price to local mills at the same level as paid to growers. While export sales prices were subject to adjustments through the season in response to a number of considerations, prices to growers were not changed after the announcement of them in order to prevent fluctuations in growers' incomes.

48. Under a new marketing strategy introduced in 1991/92, internal trade is liberalized. The role of the private sector in the production, marketing, ginning and exporting of cotton is to be greatly enhanced and a spot Cotton Exchange is to be opened. An export allocation is to be released whatever the size of the crop or the local mill requirements. The additional needs of local mills for shorter staple cottons are to be met by imports. Export policy and prices are to be announced during September of each year. Export selling prices are to be established at a realistic and competitive price level, keeping the normal differences with other international growths and taking into consideration prevailing world prices. The price differential between ELS and long staple cotton is to be narrowed. Prices paid to growers are to be fixed and announced at an early stage at levels remunerative to the grower and in line with international cotton prices.

2. Mexico

49. Mexico's production of cotton in 1992/93 was only 8.5 per cent of the level in 1980/81 as harvest area fell drastically but was partly offset by a large increase in yield. In the intervening years, wide variations in area and production were closely related to fluctuations in market prices as farmers reacted to prices in one season when making decisions on planting for the next season. Market conditions and prices changed from season to season and this created difficulties when growers had planted a large crop in anticipation of

good prices but were disappointed by what turned out to be low prices when the crop was sold. These experiences have had a negative effect on the country's financing programmes and marketing policies for cotton over the past decade.

50. Mexico's exposure to world market conditions and price levels has intensified since 1985 when, not only was there the traditional link through exports, but the Government lifted controls on the cotton trade and exempted this raw material from the requirement of advance permits to import and export it. Since then, imports have risen to a level equivalent to 15 times exports as production dropped to a very low level and consumption was sustained.

3. Pakistan

51. Cotton production and manufacturing are an important part of the Pakistani economy. Cotton and cotton-based goods account for 60 per cent of the country's earnings.

52. Pakistan's cotton production tripled from 1980/81 to 1992/93, mostly through increases in yields while expansion of area was large too. Through the 1980s and to 1992/93 exports of raw cotton have fluctuated greatly but both production and exports of yarn and fabric increased steadily and greatly.

53. Exports of raw cotton were nationalized in 1973 and the Cotton Export Corporation (CEC) was set up as a public sector enterprise. The CEC eliminated elements of uncertainty previously prevailing in the minds of foreign buyers about assured supplies of desired qualities. Subsequently, the CEC was given further responsibilities of implementing the Government's cotton policy, price support operations to protect interests of growers, ginners, textile mills and all sectors of the trade, and operations of quality improvement, ginning schemes and institutions as well as construction of modern storage facilities.

54. In 1987, the Government partially deregulated the export trade in raw cotton. Whereas previously the export trade was exclusively handled by the CEC, private sector exporters were allowed to participate in exports in competition with CEC. Private exporters were, however, required to purchase stocks from the CEC to meet their export commitments and the CEC remained responsible for the quality of cotton supplied to the private sector. Other changes were a minimum export price set by a committee and later by CEC alone, and registration of all export contracts. Later, the CEC was allowed to sell nearer to the minimum export price in cases of large volume or sales to spinners.

55. The objectives of the partial deregulation of the trade in exports of raw cotton in 1987 were as follows:

- To employ the private sector to help augment the operational capacity for efficiently handling the increasing exportable surpluses;

- To create a healthy competition between the CEC and the private sector for obtaining better prices in the export market;

- To ensure greater participation of the private sector so that exports may not remain confined in a few hands;

- To find new markets/buyers and help diversify exports of cotton.

56. The CEC's role presently is quite distinct from the private sector's roles, as the CEC, in addition to its commercial side in export of raw cotton, is still a Government agency responsible for stabilizing the domestic cotton market and ensuring minimum prices to growers and ginners through its procurement operations besides carrying out Government directives related to cotton policies from time to time. As a result, growers and ginners have received higher than the officially announced minimum prices.

57. The assured price system was introduced in 1976/77 and, since then, the area under cotton has been steadily increasing. Presently, the Government fixes assured minimum prices of seed cotton every year taking account of cost of production, competitiveness of cotton with other crops, viability of the textile industry and world cotton prices. Announcements of assured minimum prices are made before sowing time in order that farmers may consider them when taking decisions on cotton production. Similarly, the price of cotton lint is assured to ginners.

58. Pakistan has had phenomenal growth in textile capacity as measured by numbers of spindles, rotors and looms in both the organized and unorganized sectors as well as in production and exports of yarn and cloth. Exports of cotton yarn increased five-fold from 1980 to 1991 and now equal raw cotton exports by weight and would be much greater than raw cotton in value terms. Exports of cotton fabric more than doubled in the period and now are the equivalent, by weight, of 35 per cent of raw cotton exports but would exceed raw cotton in value terms. Moreover, textile production increased by 48.5 per cent in 1991 and exports by 24.8 per cent in the year.

59. Pakistani fibre is known for its good qualities, particularly strength, but its intrinsic qualities suffer from improper grading and standardization of lint. The country suffers estimated losses of 10 to 20 per cent of the true commercial value of its raw cotton exports because of poor quality control and inability to adequately separate cotton lots according to grade and staple standard. Efforts are being made to alleviate these problems through training and other activities of the Pakistan Cotton Standards Institute.

4. Peru

60. Four varieties of cotton are grown in Peru. The most widespread is Tangüis with a fibre length of 1-3/16 inches. Another is Pima with a staple 1-9/16 inches long and sometimes as long as 1-11/16 inches. A third is Aspero which, despite being a very small part of the crop, is significant as it may be grown in the jungle of San Martín Department (Huallaga area) as a competitive crop which could contribute to the eradication of the cocoa leaves grown there, while Aspero has wide acceptance in Europe and Japan because of its high absorbency. Del Cerro is the fourth variety representing a tiny part of the crop.

61. Two-thirds of the cotton production is Tangüis and a little less than one-third is Pima. As Tangüis is used relatively more by the country's mills, exports of it are a little more than one-third of total cotton fibre exports while Pima accounts for a little more than half. By value, Pima represents almost two-thirds of the total as it commands a higher price than Tangüis.

62. In 1983, cotton trade was liberalized after 8 years of a State monopoly. The economic measures adopted by the then new Government gave hopes for increases

in purchasing power of the population and reactivation of the Peruvian textile industry, and gave an encouraging perspective for the textile industry.

63. By 1991, a free market policy had eliminated controls and export sales registrations for exports of raw cotton. However, both crop production and the textile industry have been affected by economic and financial difficulties and the political situation in the country. Drought accompanying the "El Niño" weather phenomena in the Pacific also reduced yields and output in recent years.

64. For Tangüis, the variety most widely used in the country's textile industry, a procurement timetable makes it possible to assign from the first months of the year, certain volume for export. All Tangüis cotton not committed to domestic users by the beginning of August is released for export. There are no restrictions on exports of extra-long and Aspero fibre.

65. Exports of cotton yarn and fabric in 1987 roughly equalled average exports of raw cotton. Since then growth of the textile industries' exports has been constrained by unfavourable exchange measures and trade barriers of importing countries. In 1987, 38 per cent of Tangüis production was exported as yarn, fabric and ready-made garments, notably to the EEC. The country's textile production from the extra-long fibre and good strength of its Pima cotton permits spinning of yarns of exceptional fineness which can be used with other fibres to make luxury goods such as lingerie, although high quality control and fashion are important factors in this industry.

5. Nigeria

66. After a decline in production, Nigeria's output rose through the 1980s but was outstripped by rapidly growing demand of the country's mills. As a result the country became a significant importer with raw cotton imports presently at about one third of domestic production. The boom in the price of oil in the early 1970s strengthened the country's currency, as an important oil exporter. This was a significant factor which made exports of cotton and other commodities uncompetitive in world markets. Other unfavourable internal factors were labour intensiveness and alternative crops which could be produced more cheaply but obtained higher prices, competition for finance, lack of improved technology and effective extension work and problems of institutionalized marketing.

67. Mill consumption increased with expansion of existing mills and installation of new ones. In 1965, there were only 51 mills and by 1985 there were 135 mills. The large and growing domestic market provided market opportunities for cotton products while there were no exports of yarn or cloth. There may, however, have been exports of ready-made clothing items.

68. The Nigerian Cotton Board was established in 1977 along with Boards for other commodities. In addition to promoting development, providing inputs and other functions, the Nigerian Cotton Board was charged with purchasing, sales and movement of cotton and cotton products to meet domestic requirements and transport to port of shipment of any surplus to such requirements. Funds for the purchase of cotton came from the Central Bank of Nigeria and loans were repaid out of proceeds from sales. Nigeria's Commodity Boards were abolished in the mid-1980s as part of the country's Structural Adjustment Policy.

69. From 1989, the Government has given priority to diversification of the production and export base and making efforts to rehabilitate and expand the non-oil sector in order to deal with the structural problem of large imports of food and intermediate goods which emerged with the oil boom, as well as to expand export earnings and stabilize them. Cotton was considered one such commodity for production and export expansion. Clearly, in the short term, increases in domestic cotton production would save foreign exchange and indirectly ease the structural import problem and foreign exchange crisis. In the long term, it may be possible to have a surplus of cotton to export as lint, yarn, cloth or ready-made apparel items, as the country has a vast agricultural potential.

IV. GENERIC MARKET PROMOTION OF COTTON THROUGH INTERNATIONAL COOPERATION

70. As preferences of consumers are a strong determinant of demand for apparel and other consumer items made of cotton, an avenue to strengthen and expand demand for cotton is through market promotion of articles made of cotton.

71. Promotion efforts may be directed at intermediary levels, such as buyers for stores or distribution chains, in trade fairs and exhibitions, trade missions and specialized trade publications. Efforts may also be aimed at the final consumer as, for example, in general media advertising and publicity or at the merchandising level in store promotion and point-of-sale advertising.

72. In the case of promotion at the level of intermediaries, the goal is to convince them that articles made of cotton are as appealing and otherwise as good or better than competitive items, and therefore will sell as well or better than them. On the other hand, generic promotion addressed to the general pubic and purchasers at point-of-sale is intended to improve the perception of the quality of the product by the consumer.

73. Because of the nature of generic promotion, quantitative assessments of its benefits are difficult to carry out. By all accounts, generic promotion has to be pursued systematically and over a long period of time in order to realize gains. Piecemeal, haphazard or sporadic activities are unlikely to succeed. In any case, promotion and improvement in quality are two of very few avenues which cotton producers can pursue to increase demand.

74. Eight cotton producing countries have supported generic market promotion of pure cotton goods in Western Europe and Japan through the International Institute for Cotton (IIC). National cotton promotion institutions, especially in the United States, have implemented their own generic programmes.

75. IIC was established as an intergovernmental body in 1966 by a group of cotton producing countries which had become alarmed at the erosion of cotton's market share by man-made fibres. Forecasts made at that time showed that cotton would lose market share at an accelerating rate unless action was taken to improve cotton's consumer appeal.

76. IIC has undertaken promotion and advertising at the levels of industry, trade and consumers to ensure that cotton's advantages, its availability and fashion appeal are known. Backstopping these efforts is technical and commercial servicing to extend technical developments and to provide market and creative information such as design, colour and style trends to the industry and trade. IIC did some technical research and development to improve cotton's performance

both in finished textiles and garments and as an industrial raw material. The planning of projects included economic and market research, evaluation of likely benefits and provision of current information for industry, trade and the media.

77. IIC's programmes were concentrated on Western Europe and Japan since these are the principal export markets of common interest to all cotton producers and where competition from man-made fibres and fashion factors are highly important.

78. As a separate area, IIC provided technical extension and commercial training programmes to developing countries to assist the development of their manufacturing bases and their export efficiency.

79. IIC's programmes have been appreciated by governments of cotton producing countries and at all levels of cotton marketing and processing. There seems to be recognition that these programmes contributed to the gains in cotton's market share from the 1960s to the present. Competition between cotton and man-made fibres still remains intense and has spread from developed to developing regions.

80. From the point of view of international cooperation on commodities in general, IIC is one of the few examples of an organization undertaking generic promotion of a commodity. Although a producer organization, IIC received funding from nine consuming developed countries as a form of assistance to developing countries. It has also received substantial practical cooperation at the national level from the industry and marketing organizations. Most of IIC's programmes have had an international component financed by IIC and national inputs from the cooperating national organizations.

81. However, IIC has run into serious financial difficulties in recent years and is in danger of ceasing altogether. Given the economic situation of most of IIC's member countries, it has not been possible for them to increase their contributions. Some developing member countries have withdrawn citing their inability to settle their obligations or questioning the possibility of finding a long term solution to the finance problem. Another concern voiced by IIC members is the "free rider" problem of few contributing while many benefit at no cost.

82. In 1985, IIC put forward an ambitious levy-based plan for financing its operation. The plan received little support from countries which were not members of IIC. IIC has since proposed that informal talks or an international debate should concentrate on how its projects should be funded.

83. As time passes, it is becoming clearer that IIC's work will stop unless a reliable, fair financing mechanism is found soon. Contributions of developed country donors or assistance from the Common Fund, although helpful, are unlikely to provide the major part of funding needed by IIC.

V. RESEARCH AND DEVELOPMENT

84. The major objectives for research on cotton production in developing countries are improved yields, insect and disease resistance, control of insect and other pests by ecologically sound methods, improved farming systems in which cotton is a component, collection and exchange of germ plasm used for breeding new varieties, development of improved fibre quality, and improved harvesting, ginning and packaging.

85. In processing, or "utilization" as it is termed, research objectives centre around improving the aesthetic and performance characteristics of articles containing cotton through modifications in the manufacturing process or in the articles, cost reduction in manufacturing of items containing cotton, development of new products utilizing cotton, improving efficiency of cotton ginning systems and the quality of cotton lint and cottonseed produced, minimizing the problems caused by impurities in cotton lint and development of processing of cottonseed into food for human and non-human consumption.

86. Much work has already been done at the international, regional and national levels on research and development. Yet, needs are enormous. While utilization research has inherent widespread applicability, agricultural research tends to be less so because of varying conditions of pests, diseases, soils, and climate. In both types of research, networking arrangements for execution of projects and programmes have the advantages of making use of existing institutions and are less costly than creation of whole new regional or world research centres. On the other hand, regional or world centres have the great advantage of bringing together specialists on a permanent working basis to consider all problem areas in an integrated approach.

87. Of particular interest at the international level is that the International Cotton Advisory Committee (ICAC) has recently become a sponsoring body for projects on commodity development in connection with the Second Account of the Common Fund for Commodities. These activities are additional to ICAC's main functions of serving as a general forum for deliberation of matters concerning cotton and assessment of the world cotton situation and outlook together with provision of statistical information on the world cotton economy. Among the project proposals and ideas which have been considered in ICAC are: a project on "Research and development of cotton production in the tropics", another for a "Binational Paraguayan-Argentine project for the prevention and control of the cotton boll weevil", and a third for "Environmentally safe integrated pest management for high quality non-sticky cotton".

88. Cotton is a crop normally associated with the fibre produced. However, it is also an important source of oil and meal made from the seed as about two-thirds of the weight of picked cotton is cottonseed. Moreover, the meal is potentially an important source of human food containing 20 per cent protein. A flour of more than 65 per cent protein has been produced from the meal. Exploitation of the meal for human food has been held back by the presence of a substance, gossypol, which is poisonous to man. Although there are technical means to remove it, they so far are too expensive for commercial application. Since world production of cottonseed is about 38 million metric tonnes, if an inexpensive method of removing gossypol could be found, cottonseed could provide a very large source of protein-rich human food which would improve nutrition in developing countries. The increased value of the cottonseed should also add to the value of the cotton crop and thus augment producers' incomes.

VI. PRICE FORMATION

89. Because of the plethora of qualities, origins and destinations, and delivery dates, there is no international exchange where contracts for cotton from many countries are openly traded by a large number of buyers and sellers in competitive conditions. Neither is there systematic collection and dissemination of data on actual transaction prices and quantities which could give transparency to the international market. However, valuable information

on prices and other market news is provided by the weekly "Cotton Outlook", published by Cotlook Ltd. Actual transaction prices are set in contracts that are negotiated between buyers and sellers in the context of their relative strengths, their marketing strategies and the market information that is available to them.

90. In addition to major international cotton traders such as Ralli Bros., Volkart Bros., Dunavant, McFadden/Valmac and Bunge & Born, there are a very large number of small often specialized firms engaged in international trade in cotton.

91. An important price indicator is the "Cotlook A" index published each week in "Cotton Outlook". The "A" index is an average of the prices of the five cheapest of 13 cottons from different countries, all of which are 1-3/32 inches in fibre length. The prices are offering prices quoted by traders for CIF North European delivery. A similar index, "Cotlook B", is published for the less widely traded short staple cottons.

92. Another main price index is the "New York Futures No. 2" price which is the price for trading contracts in a particular cotton (SLM 1-1/16 inch United States grown white cotton) on the New York Cotton Exchange. The New York futures price is important as it gives an idea of the level of cotton prices in the next 17 months since contracts are traded that far ahead in time. The contract is also, of course, the main tool for hedging and speculating operations in cotton.

93. A new "World Cotton Futures Contract" was introduced for trading on the New York Cotton Exchange on 1 October 1992. The primary motivation for the new contract is its potential use by non-US cotton producers and users who are unable to use the New York Futures No. 2 contract to manage price risk when cash prices outside and inside the United States move in different directions or at different rates. The differences in price movements may be due to different perceptions of influences of various market factors, the operation of the United States' cotton policy or changes in transportation cost in world trade. The new contract is based on the Cotlook A index which is denominated in US cents per pound for CIF delivery in Northern Europe.

94. The World Cotton Futures could some day become a new tool for price discovery for non-US cotton. Due to its only recent introduction and light trading so far, it has not yet achieved such a status. Before its introduction, some participants in the futures market estimated that daily trading volume would need to rise to 1,000 contracts and open interest would need to increase to 5,000 contracts to ensure sufficient liquidity and the success of the contract. During the first four months of its trading, the daily volume of contracts traded averaged less than 200 and open interest on 20 January 1993 was only 1,366 contracts. In comparison, daily volume of the long-established No. 2 contract averaged about 6,000 contracts traded and open interest on 20 January 1993 was 43,406 contracts, indicating much more liquidity and depth to the market than for the World Futures contract. Over time, the participants in international cotton trade may become more accustomed to using the contract and its trading volume may rise.